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FOREIGN DIRECT INVESTMENT AND RETAILING IN INDIA-ISSUES AND CONCERNS

K. BABY
ASST. PROFESSOR
GOVT. COLLEGE
CHITTUR

C.A VISALAKSHI
ASST. PROFESSOR
GOVT. COLLEGE
CHITTUR

ABSTRACT

India enjoys a strong position as a global investment hub with the country registering high economic growth figure even during the peak of financial meltdown. As a result the investors rested their confidence in the economy which eventually pushed Foreign Direct Investment (FDI) in India. The retail industry in India has come forth as one of the most dynamic and fast paced industries with several players entering the market. But all of them have not yet tasted success because of the heavy initial investments that are required to break even with other companies and compete with them. The Indian retailing industry is gradually inching its way towards becoming the next boom industry. Successful retail organizations must understand their market, their customers and the importance of strategic location. Because of completion in the retail industry can be fierce, such organization need the best micro marketing tools available to analyse where to place new stores, establish customer profile, and determine best marketing practices in order to find new customers. Attracting FDI and forging more effective international linkage is the key to this objective. If there are policy obstacles, efforts should be made to overcome these in other ways.

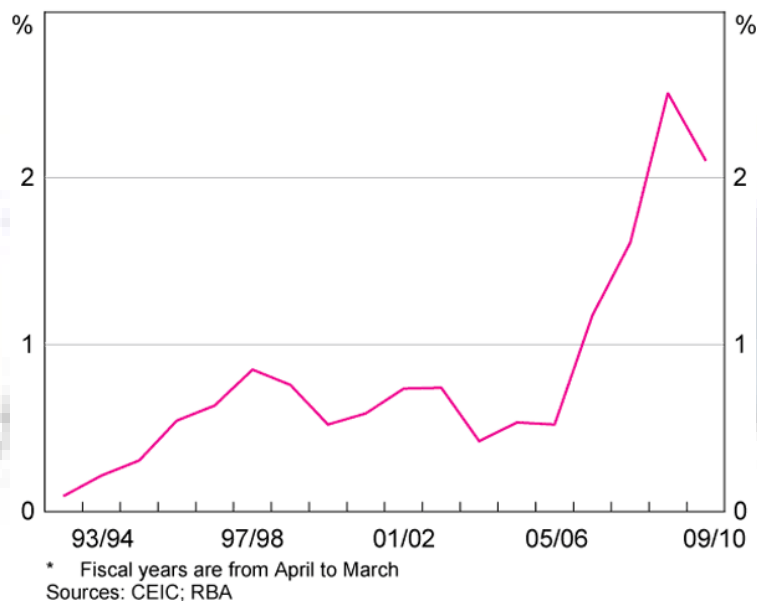
KEYWORDS

Capital flows, FDI, GDP, Investment Options, Retailing.

INTRODUCTION

The Indian investment scenario has undergone quick transformation in the post liberalization phase. India was ranked the ninth most attractive investment destination and is considered as an ideal destination for investment on the back of vibrant democratic setup. Presence of a vast network of bank branches, financial institutions, and a well organized capital market. The new regime did away with licensing, capital controls, quantitative restrictions on imports and decontrolled interest rates and reduced restriction on foreign imports. There fore these led to a noteworthy improvement in the investment climate creating incentive for private investors, both domestic and foreign. Moreover Central and state government continued to offer a number of incentives for investment projects as a result the share of private investment rose sharply from 12.5 percent of Gross domestic Product (GDP) in the eighties changed to 15.4 percent in last decades. India is gradually emerging as a popular investment destination because of quick paced economic growth and with more and more companies scaling up in small cities and towns, according to the investors at the recent India Economic summit of the world economic Forum in Mumbai. Other factors contributing to growth comprise an expanding middle class, a large population with its major chunk aged 15-35 years and increasing urbanization, investors felt that it is difficult to be bullish on investment opportunities in the short term, but India is extremely attractive from a long term perspective

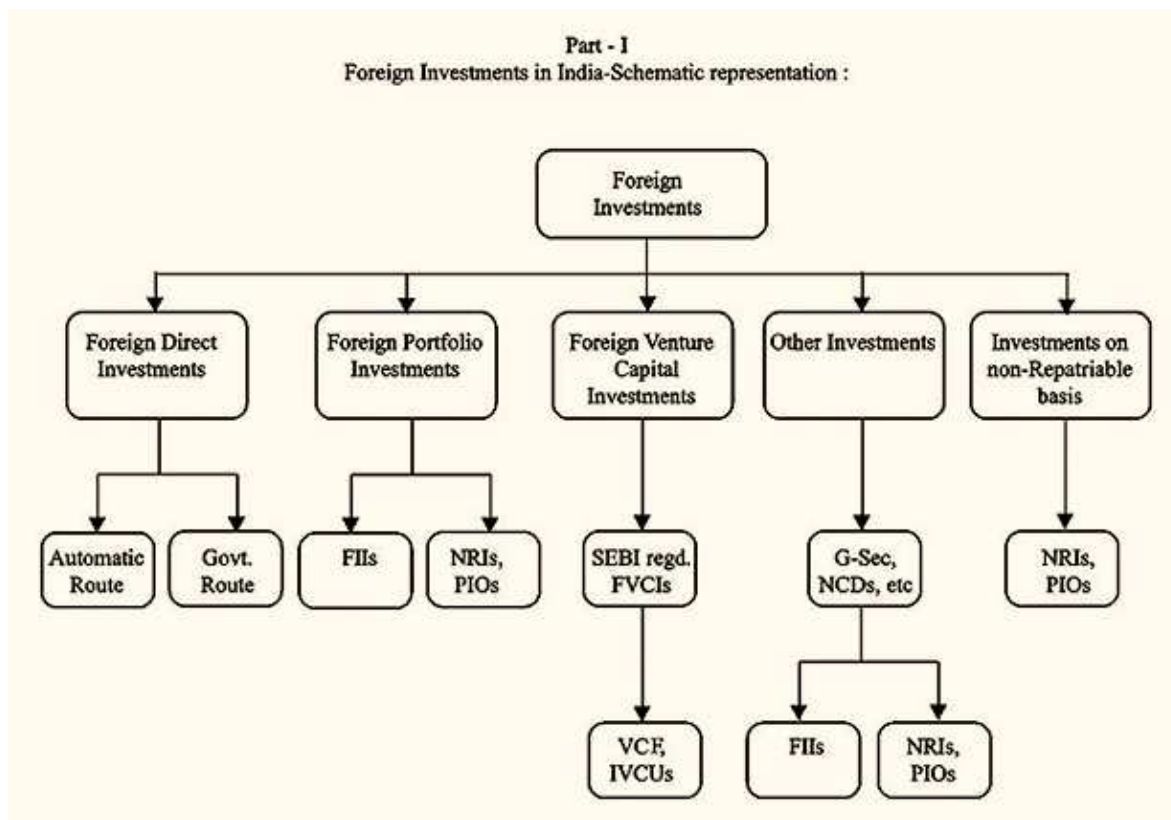
India – FDI Inflows
Share of GDP*



INVESTMENT OPTIONS

There are various investment options available in India. The different domestic investment options in India includes Bank Fixed Deposits (FD), stock market, Mutual funds, National Saving Certificate (NSC), gold, real estate, equity and many more. Retailing is considered one of the largest industries in India .It has emerged as one of the most dynamic and past paced industries with several players entering in the market. Retail industry in India is expected to rise by 25% yearly as it is being driven by strong income growth, changing lifestyles, and favorable demographic patterns. Shopping in India has witnessed a revolution with the change in the consumer buying behaviour and the whole format of shopping also altering the growth of retail industry. An important aspect of the current

economic scenario in India is the emergence of organized retail. In recent years there has been considerable growth in organized retailing and has gained momentum. Major industrial houses have entered this area and have announced very ambitious future expansion plans. In India there are multi stored malls, huge shopping centers, and sprawling complexes which offer food, shopping, and entertainment, all under the same roof in the urban land scape across the country. Various investment options are given below.



FOREIGN DIRECT INVESTMENT (FDI) IN INDIAN RETAILING

Foreign companies would be allowed to own a majority share in Indian outlets conducting multi-brand retail trade. At political level it is approved that 51% shares for foreign companies. While commending India to go ahead with 'strategic Alliance with the US', which urged the Indian leaders to speed up the entry of foreign multi brand retail giants like Wal-Mart, Carrefour and Tesco into Indian retail trading of all products, including grocery, food and other consumebales. At present the foreign companies are only permitted to operate cash-and carry format stores catering to whole salers and business consumers. As a sop to critics, the committee has laid down the condition that foreign retailers should dedicate at least 50 percent of their proposed investment to back-end supply chain infrastructure. They would further have to commit a minimum of \$100 million. However, the demand from the domestic retailers that the foreign retailers should sell at least 30% of their total turn over to local retailers either as wholesaler in the cash-and carry model has been rejected. Another proposal to force the foreign retailers to source merchandise from the domestic small and medium scale producers need to be examined to see if it meets with the WTO norms. It is a fact that the entry of foreigners with their vast organizational power would seriously affect the domestic labour market has more than a grain of truth and it would ultimately lead to unfair competition and result in large scale exit of domestic retailers, especially small family managed outlets, leading to large scale displacement of persons employed in the retail sector.

INDIAN RETAIL SHOP



IMPACT OF RETAILING

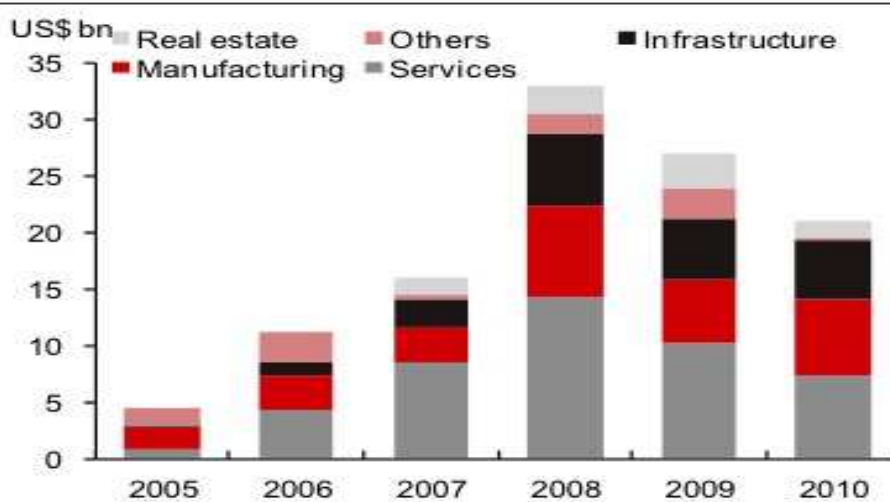
No one can deny the fact that the present retail sector is unorganized and the multiple point of sale between the farm-gate and the consumer leads to wide disparity between the price paid to the farmer, and the one paid to the consumer, but the setup also provides job to millions. The organized retail would control prices and contain inflation as is voiced by the reformers is unlikely to happen in India. Once they enter the country and setup shop, global retailers with their enormous monopolistic power to manipulate the markets can actually pay less and charge more. Also the big foreign retailer would have necessarily operated in urban milieu because he needs a large market and whatever benefit he would be for the urban elite. This surely would lead to further urban- rural socio economic tensions.

FDI IN SERVICE SECTORS

In India the service sector accounts for 55 percent of India’s Gross Domestic Product. It growing by 10 percent annually, contributes about a quarter of total employment and over one-third of total exports and then is growing at a fast rate. It is emphasized that we have to sustain a high growth of the service sector. It is true to say that to tap the full potential of the service sector, policy reforms are needed. Among the various policy reforms, the single one that can contribute most to the further growth and maturing of India’s service sector is making it easier for foreign direct investment in services. However the issue has become intensely contested. FDI window into services has been opened only slightly. Many areas of the services sector are altogether out of bounds for the foreign direct investment. But despite severe restrictions, the service sector has attracted not less than 44 percent of the total FDI equity flows between April 2000 and December 2010 in only four sectors, namely financial and non financial services computer hardware and software, telecommunications, housing and real estate. If the construction sector is included then the share of the service sector in the total equity flows will jump to 51 percent. Of these sectors financial and non financial companies have attracted the largest FDI equity flow with a share of 21 percent .Larger FDI flows can radically improve some of the India’s critical services sector and help overcoming the challenges that are before India’s service economy to day. The Economic Survey of 2010 clearly pointed out that the three challenges

FDI SECTORAL COMPOSITION IN INDIA 2005-10

Figure 1. FDI inflows by sector

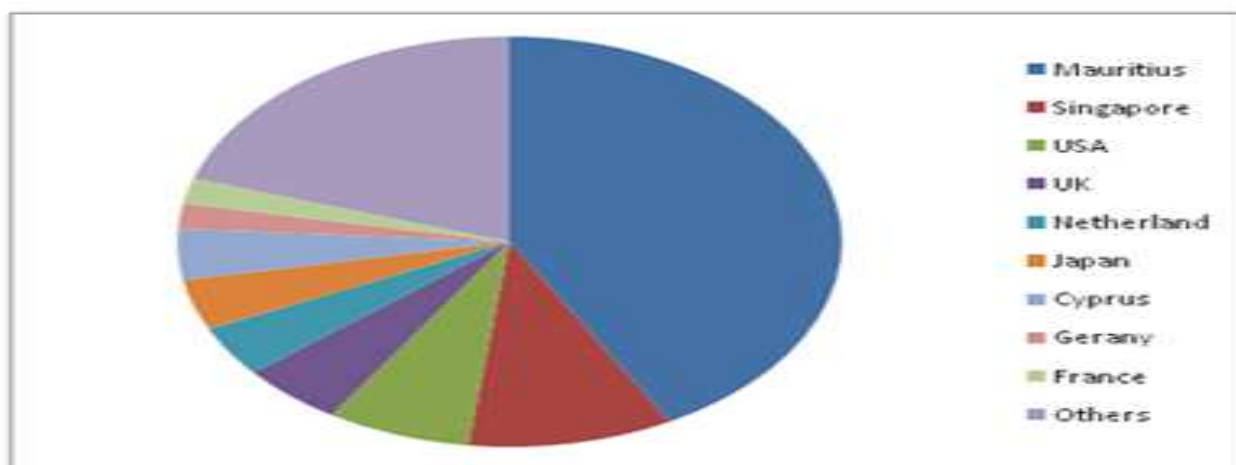


Source: CEIC and Nomura Global Economics.

CHALLENGES

- The biggest challenge is to retain India’s competitiveness in those sectors where it has already made a mark such as IT and communications.
- The second challenge lays making inroads in traditional services, such as tourism and shipping and other countries have already established themselves.
- The third is to make India’s presence felt in globally traded services such as financial services, health care, education, accountancy and other business services.

FOREIGN DIRECT INVESTORS IN INDIA



It should be noticed that greater integration with large global players through investment and international relationship building could help in overcoming these challenges and making India a service super power. Indeed the opportunities in this fast growing employment oriented sector are sticking. But allowing greater FDI into these activities is fraught with policy restriction. In the case of retail trade, FDI is prohibited excepting in single brand retailing subject to a 51 percent cap. FDI in cash and carry wholesale trading is however permitted. During the period , April 2006 to March 2010, FDI inflows into retail amounted to just about

195 million dollars accounting for 0.21 percent of total FDI flows during the period. FDI in retail is permitted in Brazil, Indonesia, Argentina, Singapore, China and Thailand with out any limit on equity participation. Permitting FDI retail in a phased manner beginning with the metros and incentivising existing retailer to modernize could help the interest of the consumers as well as farmers. FDI in retail can bring in latest technology and supply chain management into the country.

FDI IN SERVICE SECTOR INFLOW (2006-2010)

Rank	sector	2006-07	2007-08	2008-09	2009-10	Cumulative Inflow (2000-2010)	%age to total inflow
1	Service sector (financial & non financial)	4664	6615	6116	4392	23640	21
2	Computer software & hardware	2614	1410	1677	919	9872	9
3	Telecommunication (radio paging, cellular mobile, basic telephone service)	478	1261	2558	2554	8931	8
4	Housing & Real estate	487	2179	2801	2844	8357	8
5	Construction (including roads & highways)	985	1743	2028	2868	8059	7
6	Power	157	967	985	1437	4627	4
7	Automobile	276	675	1152	1177	4565	4
8	Metallurgical industry	173	1177	961	407	3130	3
9	Petroleum & Natural Gas	89	1427	412	272	2666	2
10	Chemicals	205	229	749	362	2496	2

Data Source: Department of Industrial Policy and Promotion, 2010
Ministry of Commerce and Industry
Government of India

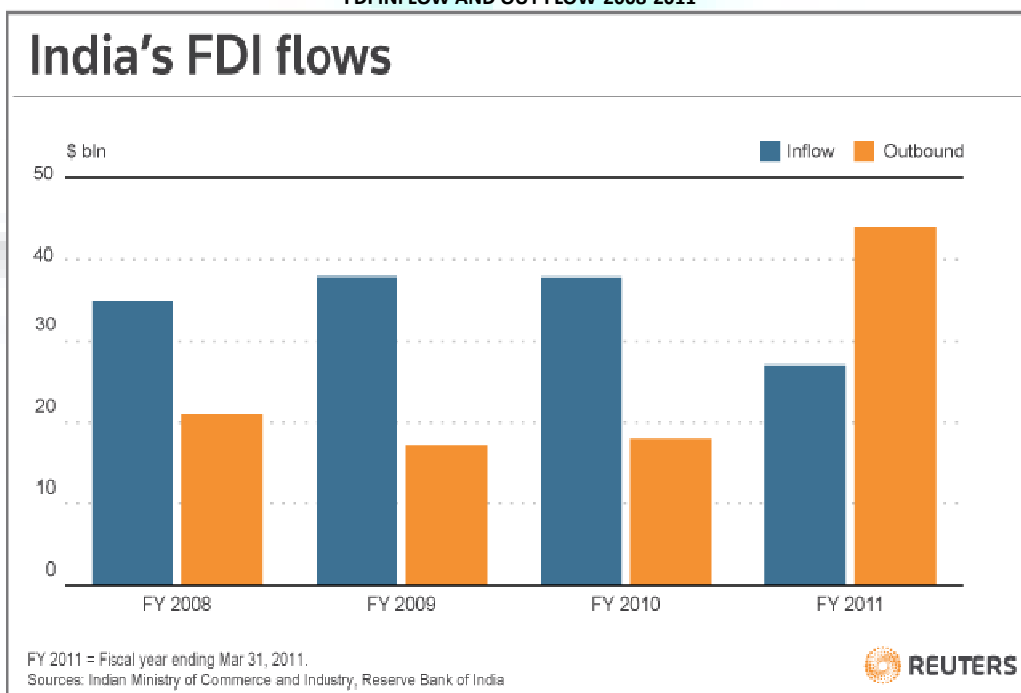
DEVELOPMENTAL CONSIDERATIONS

In the late 1990s the retail sector has witnessed marked transformation. Retailing is perceived as a beginner and as an attractive commercial business for organized business i.e. the pure retailer is began to emerging now. Organized retail business in India is very small but has tremendous scope. The total in 2005 stood at \$ 225 million, accounting for about 11 percentage of GDP. In this total market, the organized retail accounts for only \$8 billion of total revenue. Organized retailing will now grow faster than unorganized sector and growth speed will be responsible for its high market share, which is expected to be \$17 billion by 2010-2011. according to Confederation of Indian Industries, in New Delhi has the good resources and good condition for the retail sector. Out of the total earnings of the Government of Delhi Rs 11000 crore, Rs 6500 crore is achieved from the retail sector.

KEY STATISTICS

- FDI inflow rose by 50 per cent to US \$ 20.76 billion during January-August 2011, while the cumulative amount of FDI equity inflows from April 2010 to August 2011 stood at US\$ 219.14 billion, according to the latest data released by the Department of Industrial Policy and Promotion (DIPP).
- Services (financial and non- financial), telecom, housing and real estate, construction and power were the sectors that attracted maximum FDI during the first eight months of 2011 while Mauritius, Singapore, the US, the UK, the Netherlands, Japan, Germany and the UAE, among others, are the major investors in India.
- India's foreign exchange (Forex) reserves have increased by US\$ 858 million to US\$ 318.4 billion for the week ended October 21, 2011, according to the weekly statistical bulletin released by the Reserve Bank of India (RBI). In the considered week, foreign currency assets went up by US \$ 861 million to US\$ 282.5 billion, while the gold reserves stood at US \$ 28.7 billion.

FDI INFLOW AND OUT FLOW-2008-2011



EMERGING TRENDS IN INDIAN RETAIL INDUSTRY

The Indian retail environment has been witnessing several changes on the demand side due to the increased per capita income, changing life style, and increased product availability. The traditional format like hawkers and grocers coexists with modern format like supermarkets and non store retailing channels such as multilevel marketing and tele-shopping. Modern stores tend to be large, carry more stocks, keeping units, and have a self service format and an experimental ambience. In recent years there has been a slow spread of retail chains in some format like supermarket, malls, and discount stores. Factors facilitating the spread of chains are the availability of quality products at lower prices. Improved shopping standards, convenient shopping and display and blending of shopping with entertainment. Cities like New York, Los Angeles, Vancouver, London, Paris, New Delhi, Mumbai etc are booming and expanding in retail business due to their strategic approach in deciding facilities, customer services, retail visual and their prompt responses on customer requirements.

DEVELOPMENT OF RETAILING

The Birlas have marked their presence by acquiring Madura Garments, while Reliance plans to develop its retail venture and fuel retail network simultaneously. Even the public sector companies like HPCL, IOCL, and BPCL realized their potential for entering in to retailing by leveraging their supply chain network. At the macro level factors such as rising disposable income, dominance of the younger population in spending, urbanization and shift of the traditional family structure towards the nuclear family are the factors responsible for the development of organized retailing in India. Being considered a sunrise sector of the economy, several large business houses are entering the retail industry under multiple modern formats. On the one hand, the advancement of information technology is improving end to end business processing by integrating the entire value chain, backward and forward, for operational efficiencies. On the other hand, rising real estate prices, infrastructural constraints, and expensive technology are making the retail industry capital intensive. The governments of India prohibit FDI in retail except for single brand joint ventures with up to 51 percent equity share. The recent growth of the retail industry has already made impact on the commercial real estate sector.

REGULATORY FRAMEWORK

As a result of shortage of land and rising property prices, finding property in commercial market is becoming difficult. The licensing process for organized retail is cumbersome requiring as many as 33 licensing protocols. Besides the lobby against modern retail is mounting in recent years from traditional retailers. Nevertheless, the macro-economic landscape indicates that the domestic retail industry has immense scope for the modern as well as the traditional retailers to coexist. Through a balanced regulatory framework and competition policy, both the traditional format and the modern format can continue to grow eventually closing the gap between the organized and unorganized retailing will promote quality employment, improve business process practices, higher investment in support industries, and enable the modernization of fragmented traditional retail industry. Modern retail business focuses on maximizing customer footfalls and capturing rising volume and shares of the customer budget. Retailing is not an activity that can boost GDP by itself. It is only an intermediate value-adding process. If there are not any goods being manufactured, then there will not be many goods to be retailed. This underlines the importance of manufacturing in a developing economy. One could argue that the alarmingly low contribution of industry is attributable to the structural adjustments going on the sector, getting rid of the flab and getting ready to compete, but that still cannot undermine the seriousness of the issue at hand, in that only 600 million is employed in organized manufacturing. The efficiency can be maintained through

- The retail sector in India is severely constrained by limited availability of bank finance. So the government and RBI need to evolve suitable lending policies that will enable the retailers to expand and improve their efficiencies.
- A National level commission must be established to study the problem of the retail sector and to evolve policies that will enable it to cope with FDI as and when it comes.
- The commission should evolve a clear set of conditionality on giant foreign retailers on the procurement of farm produce domestically manufactured merchandise and imported goods. This conditionality must be aimed at encouraging the purchase of goods in the domestic market, specify the details of standard to be maintained.
- Entry of foreign players must be gradual and with social safeguards so that the effects of labour dislocation can be analysed and policy must be implemented to control predatory pricing
- There has been a substantial fall in employment in the manufacturing sector. So it is imperative to develop and improve manufacturing sector to absorb the misplaced labour force.
- The government must encourage setting up of co-operative stores, ware housing units and cold chains to procure and store their consumer goods and thereby lowering the capital cost for small retailers. From small producers for addressing the dual problem of limited promotion and marketing ability as well as market penetration for the retailer

IMPACTS OF ORGANIZED RETAILING

Organised retailing in India is gradually inching its way towards becoming the next boom industry. The whole concept of shopping has altered in terms of format and customer buying behaviour, ushering in a revolution in shopping in India. The Indian corporate retailing sector is at an inflexion point where the growth of organized retailing and growth in the consumption by the Indian population is going to take a higher growth. The emergence of organised retailing has given rise to the need for a whole new set of business skills and competencies required to efficiently manage organized retail operations. Among the many issues, values of assortment, purchase experience, logistics and supply chain issues, financing options, channel consolidations, volume driven relationships and people strategies have acquired completely new dimensions.

NEED FOR ORGANISED RETAILING

The Indian retail sector is highly fragmented, consisting predominantly of small, independent, and owner managed shops. And most of the parts are untouched by corporate business principles. It was only in 1980s when the economy was opened, the situation began to change. Companies like Bombay Dyeing, Raymond and Grasim from the textile sector were the first ones from the corporate world to step into the retailing by opening their own outlets. Titan's another successful story of a corporate creates a great retailing concept, by establishing a series of elegant watch showrooms across the country. The post liberalization era witnessed new wave of entrants in the sector with large scale investment like Tatas, the RPG Group, Rahejas and the Piramals investing in the sector. Various other Indian corporate sectors like the Birlas, the Hero group, and the Reliance have expressed their intention of joining the Indian retail foray.

FOOD RETAIL SECTOR

The food retailing industries in India presents a focused opportunity to the government to catalyze growth and employment. It is a fact that with 3.6 million shops retailing food employing 4 percent of total work force and contributing 10.9 percent to GDP. The food retail sector can be improved through

- Provision of training in handling storing transporting storing grading maintaining hygiene standards by adopting appropriate measures.
- Creation of infrastructure for retailing at community centers in a hygienic way will enable greater employment and faster transport
- Quality regulation through certification and price administration bodies can be created at for upgrading the technical and human interface in the rural and urban supply chain
- Credit availability for retail traders must be encouraged with view to enhancing employment and higher utilization of fixed assets which would lead to less wastage.

- Integrating very long food supply chains in dairy, vegetables, fish, and fruits have been evolved in India. This integration of food supply chain will provide new products in new markets increasing consumer choice economic activity and employment.

PROSPECTS OF RETAILING

Indeed, the entry of large organized retail chain could benefit the small farmers to the unemployed youths in cities and towns. The government is reportedly working out a set of rules for operation of foreign retail chain. These will understandably include requirements of local procurement. As per the set rules it is said that the retailers will be obliged to procure at least 30 percent of their requirements locally. It could infact help export from the small sector. Besides the large retailer could help in stabilizing prices by going directly to the farmers for purchase of food, vegetables etc and thereby cutting out tiers of middlemen. In the case of banking there is the scope for attracting large investment from abroad and the issue of changing the relevant laws has been discussed threadbare. Presently foreign investment of 74 percent is allowed. Admittedly in the light of global financial crisis, the issue relating to FDI in banking and further liberalizing operation of foreign banks will have to be seen in the context of overall financial stability. In India banks are sound but there is no doubt that export of financial services could be increased substantially through global linkage. In this context, the principal of reciprocity could also be applied to countries that have allowed Indian banks to expand.

CONCERNS OF RETAILING

- Most of the consumers feel that the small scale retailers put in the more efforts to maintain good relation with the consumers. The organized retail outlet should consolidate their position by strengthening the advantages and the sector has to put more efforts to maintain good relation with the consumers.
- The message conveyed to the target consumers must be effective enough in differentiating the retail outlets offering them that of its competitors with out even naming them.
- The organized retailers have to give more emphasis on display visual communication strategy might be planned and also be brand positioned.
- Critical components of supply chain planning applications can help manufactures meet retailer's service level and maintain profit margins. They have to develop innovative solution for managing the supply chain problem.
- Retailers benefit only if consumers perceive their store brand to have consistent and comparable quality and availability in relation to branded products.

RETAILING AND EXCLUSION OF THE POOR

The real world does not always confirm to the finest rules of the market and optimality. The market efficiency brought in by the global value chain is most likely to drive out small and resource poor farmers, as happened during the proliferation of the retail giants in the presently developed economies. A direct implication of such an eventuality is formulation of policies that promote large scale farming and corporatisation so as to overcome the disadvantages of small scale farming. This may lead to displacing the poor from their land base and making them dependent on market forces is a tricky situation, especially when no other form of social protection is in place to take care of the interest of the poor. In the concern about resource sustainability, equity and food security of the poor will also receive their rightful consideration in the policy formulation, especially when food inflation in the country continue to push many poor to reduce their food intake both in terms of quantity and quality. It is thus important to shift the locus of the discourse on global value chain from its central thrust on the emerging middle class to addressing the larger developmental issues including that of employment generation and effective demand for the poor. This is particularly important because of the poor and their exclusion from development as well as market is a reality in India.

CONCLUSION

At present the organized retailing in India is witnessing considerable growth. A number of large domestic business groups have entered the retail trade sector and are expanding their operation aggressively. Several format of organized retailing like hyper market, supermarkets and discount stores are being set up by big business groups besides the ongoing proliferation of shopping malls in the metros and other large cities. Organised retail business is perhaps the best news for India's retail revolution. International consultants have declared India to be the world's second most attractive destination for retail investment after Russia. The retail industry in India has come forth as one of the most dynamic and fast paced industries with several players entering the market. But all of them have not yet tasted success because of the heavy initial investments that are required to break even with other companies and compete with them. The Indian retailing industry is gradually inching its way towards becoming the next boom industry. Successful retail organizations must understand their market, their customers and the importance of strategic location. Because of completion in the retail industry can be fierce, such organization need the best micro marketing tools available to analyse where to place new stores, establish customer profile, and determine best marketing practices in order to find new customers. Attracting FDI and forging more effective international linkage is the key to this objective. If there are policy obstacles, efforts should be made to overcome these in other ways. India enjoys a strong position as a global investment hub with the country registering high economic growth figures even during the peak of financial meltdown. As a result overseas investors rested their confidence in the economy with which eventually pushed Foreign Direct Investment (FDI). Considering the pace of FDI growth in India; it is believed that FDI in 2011-12 may cross \$35 billion.

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